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120 PARK AVENUE, NEW YORK, NY 10017-5592

TO: DISTRIBUTION **DATE:** August 18, 1992

FROM: Marketing Information & Analysis / Jeanne Kiernan

SUBJECT: BLACK & WHITE/PRIVATE LABELS

In May 1992, Black & White/Private Labels overtook Branded Generics as the largest discount category segment. The following analysis examines the segment's dynamics including pricing, distribution and competitive environment.

CONCLUSIONS

- B&W's decision to reposition Raleigh Extra to the BW/PL price point may provide the company with an opportunity to regain its leadership position in the BW/PL segment. Raleigh Extra is a legitimate brand with attractive packaging, and it has higher distribution than any other BW/PL at 69%.

- The repositioning of Raleigh Extra to the BW/PL price point, combined with the introduction of the "brands" Monarch and Private Stock, confirms the "branding" of the fourth tier. In fact, even prior to Raleigh Extra's repositioning, 48% of BW/PL smokers identified their BW/PL brand by name rather than as a price point, according to Continuous Tracking.

  This suggests that although a retail outlet may have its own private label, it may be willing to carry other BW/PL brands to satisfy consumer demand. With more than one BW/PL brand per outlet, price competition will likely increase, driving prices downwards.

- Half of PM's national BW/PL retail volume, and 58% of its volume in Convenience outlets in May was from Private Labels. Reliance on Private Labels may be problematic to PM because growth through multiple brands with limited distribution is contrary to the industry trend of "branding" the fourth tier. While providing retail direct accounts with their own Private Labels may enable PM to capture low end volume in particular outlets, PM may be missing an opportunity to be among the first to establish a widely available BW/PL "brand."

- Since March 1992, RJR has become an aggressive BW/PL competitor, gaining +10% distribution nationally, and +0.6 share points, the same share increase as PM. RJR appears to be targeting pack outlets and Regions 1, 2, and 3 for BW/PL development. Such a strategy takes advantage of limited BW/PL competition in Regions 1 and 2 (SDIs of 58 and 57, respectively). In addition, by focusing on Convenience stores, RJR is capitalizing on Best Value's strength there, and the high volume potential for this trade class.

  With the introduction of Monarch and strong support for Best Value, RJR may have a two-pronged strategy:

  - Shape the industry with an attractively packaged "brand" (Monarch). RJR may be attempting to achieve first mover advantages by being the first manufacturer to offer a product at the lowest price point with attractive packaging, and a name that does not sound "cheap." However, because Monarch has been rolled out slowly, the newly repositioned Raleigh Extra may pre-empt any first mover advantages anticipated for Monarch.

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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

- Take advantage of existing Best Value distribution, and compete against other existing BW/PL brands in the industry as it is today. By using Best Value, which currently has unattractive packaging and a name that suggests low price, RJR can compete head on with existing BW/PL brands which are similarly packaged and named. As the tier develops and attractive brands are demanded by consumers, RJR will be able to replace Best Value distribution with Monarch distribution.

- PM's wholesale private labels may be at a disadvantage relative to RJR's BW/PLs in net pricing to retailers. Although both manufacturers pay the trade (wholesalers and retailers) a total of $1.60/carton, PM pays the entire amount to wholesalers, while RJR pays only $0.50 to wholesalers, and $1.10 to retailers. As a consequence, if a wholesaler tries to match RJR's payment to the retailer ($1.10), the wholesaler will only make $0.50, the same amount as he would make selling RJR's products or Basic. This low return to the wholesaler will not provide incremental compensation a wholesaler would expect for having marketed the product. Therefore, wholesalers may be more motivated to push distribution into outlets not previously having BW/PLs, than to attempt to compete on price in outlets which carry RJR BW/PLs.

  In competitive situations, if PM's wholesale partners do not meet RJR's retail payment, PM's wholesale private label brands may lose distribution and share. Although in these outlets, the retail prices for PM wholesale private labels and RJR BW/PLs may be the same, if RJR's products are more lucrative to the retailer, they will likely be given better visibility, translating into higher share.

- Premium price increases and BW/PL price decreases combined with growing BW/PL distribution appear to have adversely impacted Marlboro. Marlboro's inter-brand alternate purchase rate has been increasing since November 1991, and BW/PLs' share of Marlboro alternate volume has been rising since December 1991.

- Because BW/PL growth is fed by a combination of growing consumer acceptance, distribution gains, and decreasing prices, BW/PLs will continue to lead Discount category growth.

FINDINGS

- BW/PLs have overtaken Branded Generics as the largest Discount category segment as reflected by both Nielsen and shipment data. National distribution for the segment increased +6% from March levels to 83% in May.

- Convenience is becoming an increasingly important source of BW/PL volume; of the Nielsen trade classes, more than half (56%) of BW/PL volume was sold in Convenience outlets in May 1992.

  PM has led BW/PL volume gains in Convenience since November 1991, accounting for 48% of the segment's share gains. PM Private Labels have been the drivers of this PM BW/PL growth, increasing +1.0 points from February to May, while Basic increased only +0.2 points. Interestingly from April to May RJR met PM's +0.6 share gain in Convenience outlets.

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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

- Deviating from their declining trends, BW/PL carton prices increased slightly (+$0.04) from 6/8 to 7/6 while pack prices stabilized. Interestingly, the carton price gap between Premium and BW/PLs stabilized at 35%, while the pack price gap widened +1% to 37%.

- Since March, RJR has been on a distribution drive in Convenience (+13%) and Grocery outlets (+14%), and in Regions 1(+10%), 2 (+14%), and 3 (+15%). While some of the distribution gains may have resulted from the launch of Monarch, most of them were due to Best Value, which gained +11% in Convenience, +13% in Grocery outlets, +9% in Region 1, +10% in Region 2, and +14% in Region 3.

- RJR and B&W have the richest offers to retailers carrying their BW/PL products: RJR pays retailers $1.10/carton, and B&W pays $1.15/carton.

- American's and RJR's Branded Discount products have become more aggressive in discounting in an apparent effort to defend the brands against losses to BW/PLs. PM's Branded Discount spending has lagged the competition.

AVERAGE COUPON VALUE	CAMBRIDGE	DORAL	BRISTOL	STERLING	MONTCLAIR
MARCH 29	$3.71	$3.69	$1.93	$1.93	$1.72
MAY 31	$3.76	$4.28	$1.99	$2.35	$2.00
CHANGE	+$0.05	+$0.59	+$0.06	$0.42	$0.28
PERCENT OF STORES WITH COUPON					
JANUARY 5	69	60	42	56	43
MAY 31	74	81	44	64	55
CHANGE	+5	+21	+2	+8	+12

DISTRIBUTION:

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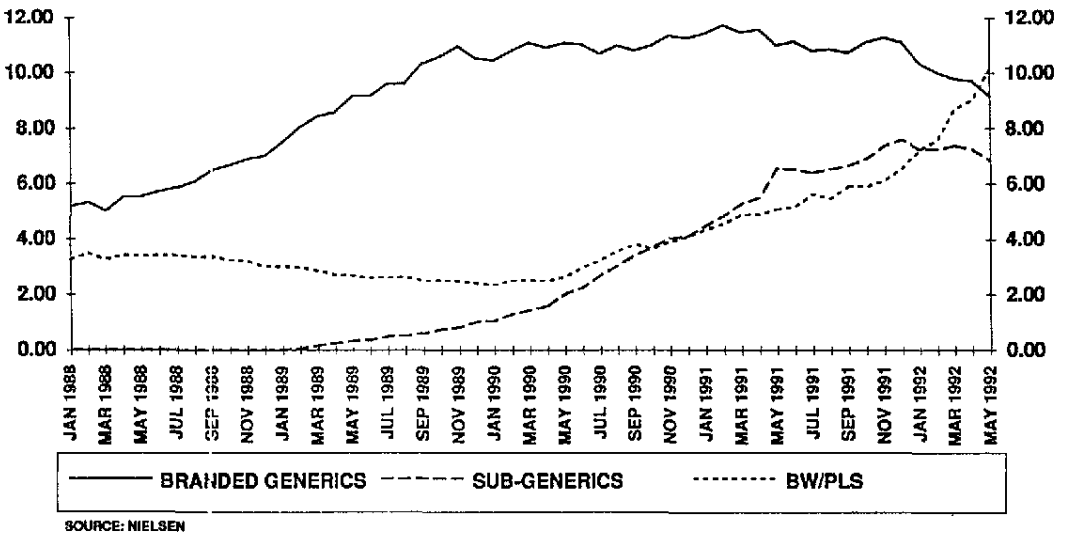
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

SHARE OF INDUSTRY

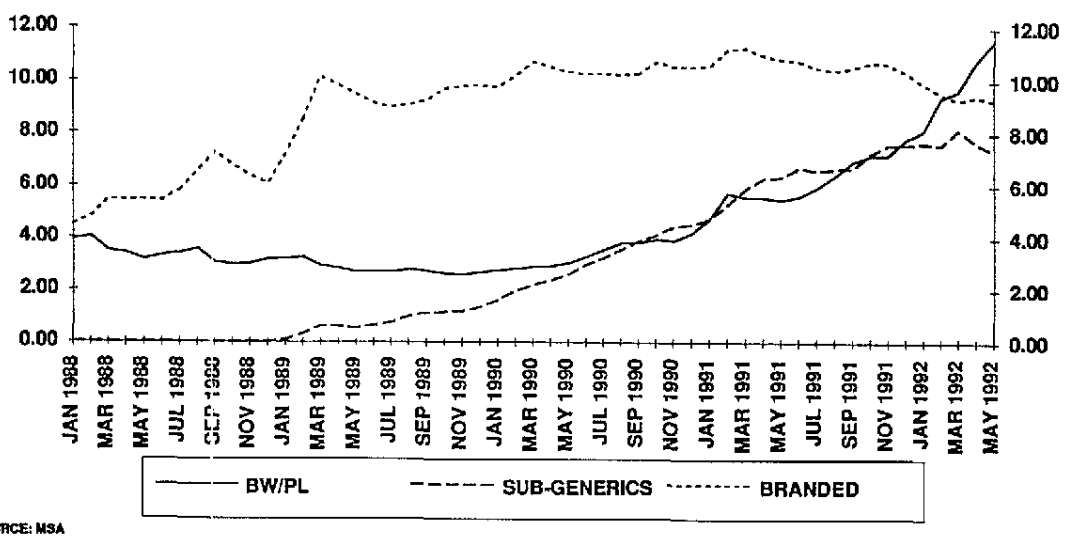
BW/PLs are now the largest component of the Discount Category, holding retail share of 10.2 in May 1992. They have led Discount category growth since January 1992. 3MM shipment data show BW/PLs as the largest segment of the Discount category since March 1992, and by May 1992, BW/PLs represented 11.5% of total industry volume (3mm).

DISCOUNT CATEGORY SEGMENT SHARE
TOTAL U.S.



SOURCE: NIELSEN

DISCOUNT CATEGORY SEGMENTS
3MM SHARE OF INDUSTRY



SOURCE: MSA

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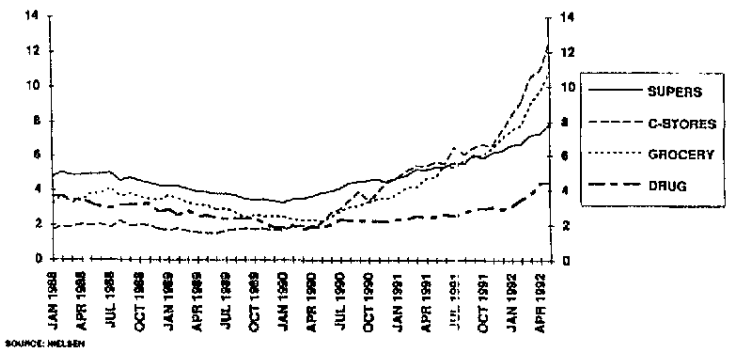
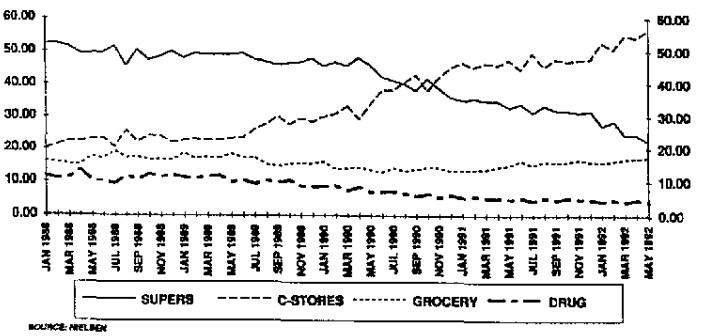
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

Convenience continues to be the most important trade class for the BW/PL segment. According to Nielsen not only is Convenience the best developed trade class for BW/PLs, but it is also the most important source of volume, accounting for 56% of Nielsen volume in the month of May 1992.

TOTAL BW/PL
1MM SHARE OF INDUSTRY

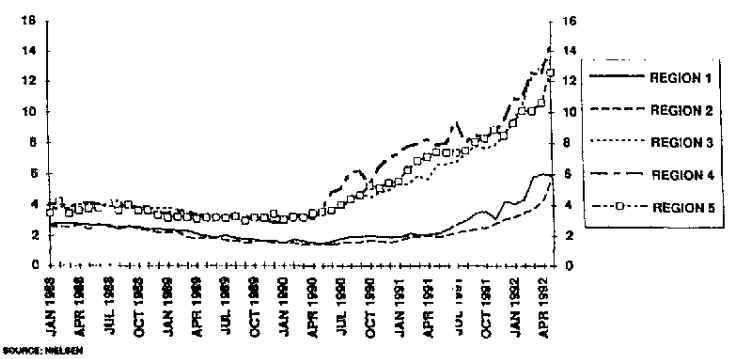


TOTAL BW/PL
TRADE CLASS PERCENT CONTRIBUTION
TOTAL U.S.

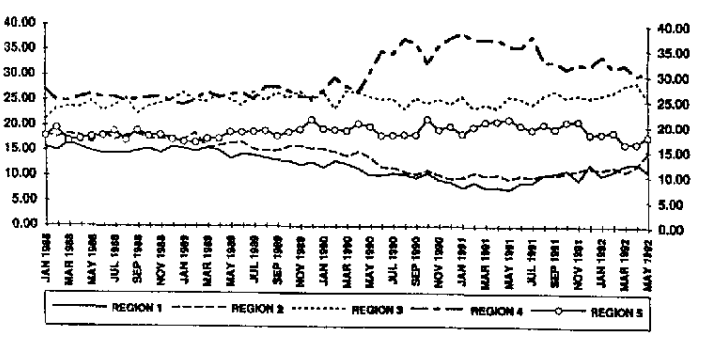


Geographically, in Regions 3 and 4 BW/PLs hold their largest share at 13.6 and 14.5, respectively. Correspondingly, they are the most important sources of volume, contributing 25% and 30%, respectively.

TOTAL BW/PL
1MM SHARE OF INDUSTRY



TOTAL BW/PL
GEOGRAPHY PERCENT CONTRIBUTION
TOTAL U.S.



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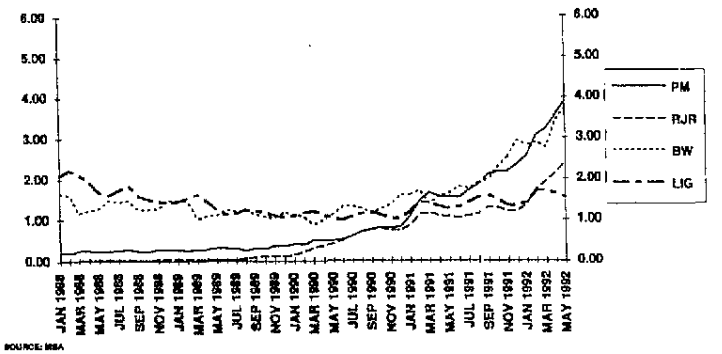
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

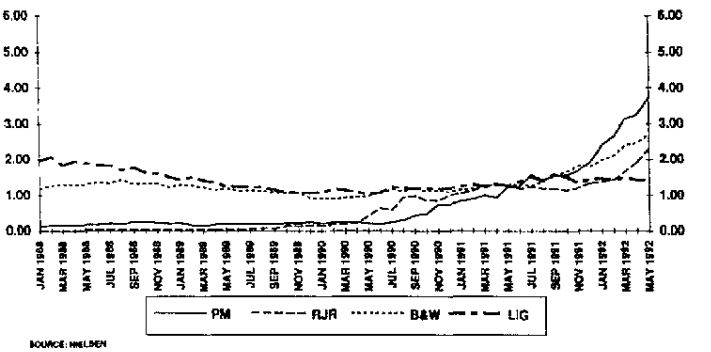
PM BW/PLs have accounted for 50% of the national BW/PL gain from December 1991 to May 1992. 3mm shipment data show PM as the leading BW/PL manufacturer since February 1992.

Since March 1992, RJR has matched PM's national retail share gains, with both manufacturers' BW/PLs gaining +0.6 points. RJR's gains have been greatest in Regions 2 (+0.8) and 5 (+1.2) since March 1992.

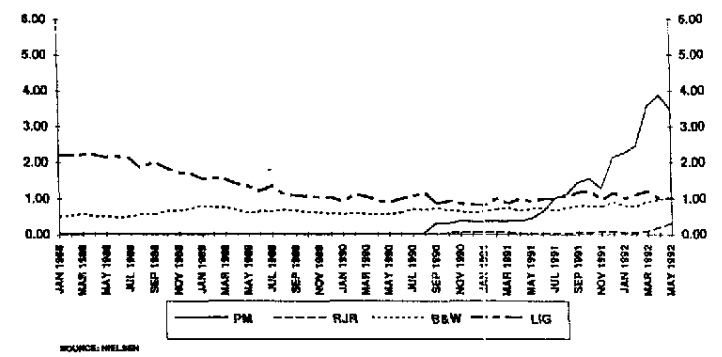
BW/PL SHIPMENTS
3MM SHARE OF INDUSTRY



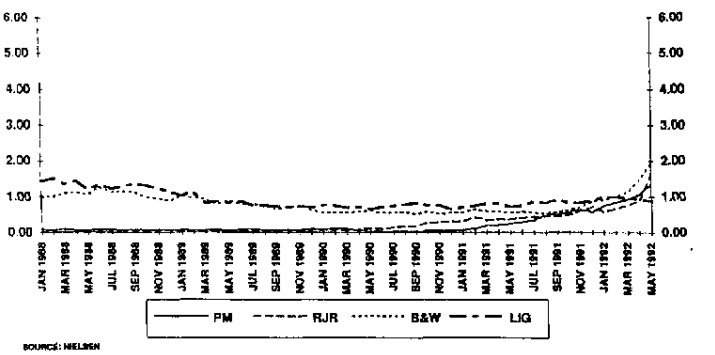
BW/PL 1MM SHARE OF INDUSTRY
TOTAL U.S.



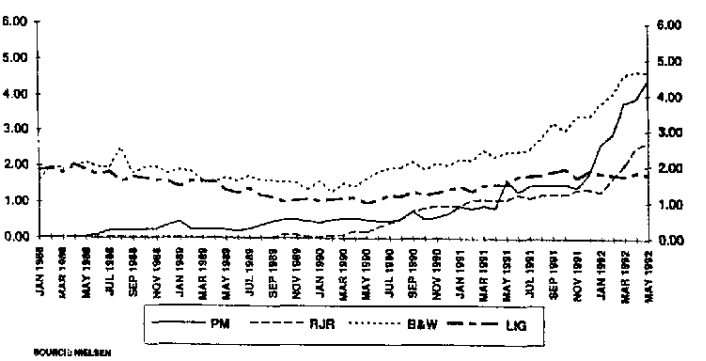
BW/PL 1MM SHARE OF INDUSTRY
REGION 1



BW/PL 1MM SHARE OF INDUSTRY
REGION 2



BW/PL 1MM SHARE OF INDUSTRY
REGION 3



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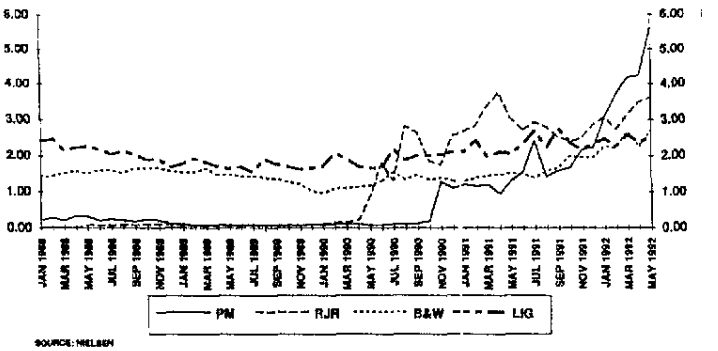
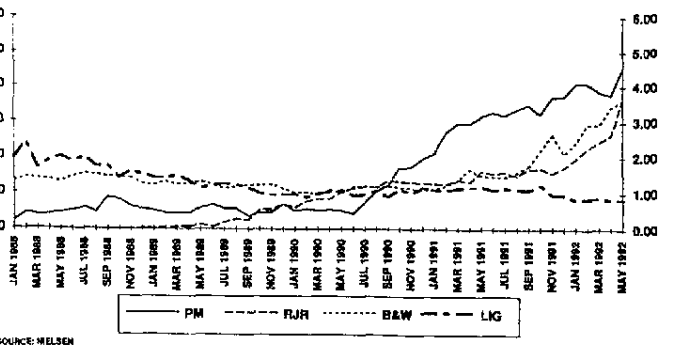
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

BW/PL 1MM SHARE OF INDUSTRY
REGION 4

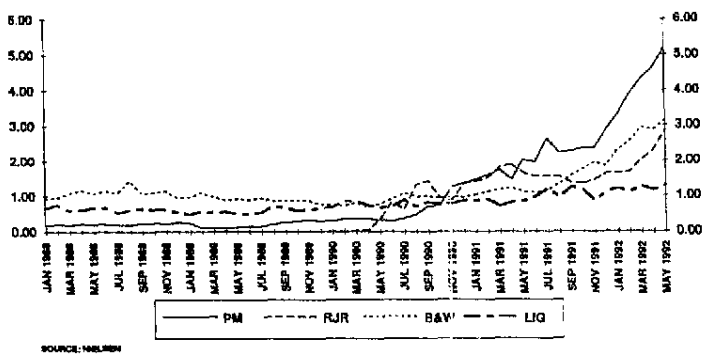


BW/PL 1MM SHARE OF INDUSTRY
REGION 5

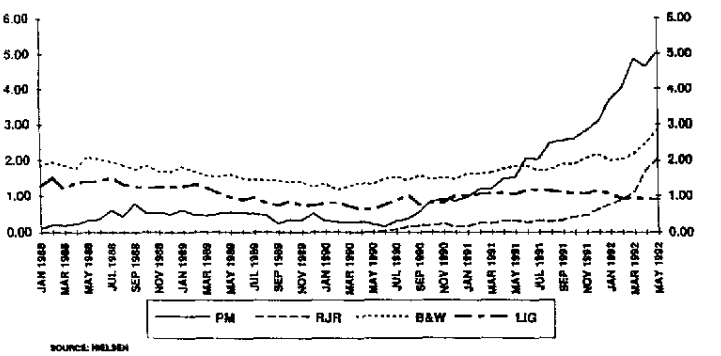


PM has driven BW/PL growth in Convenience outlets since November 1991, accounting for 48% of the tier's share gains. Note RJR's April to May share increase was the same as PM's, +0.6.

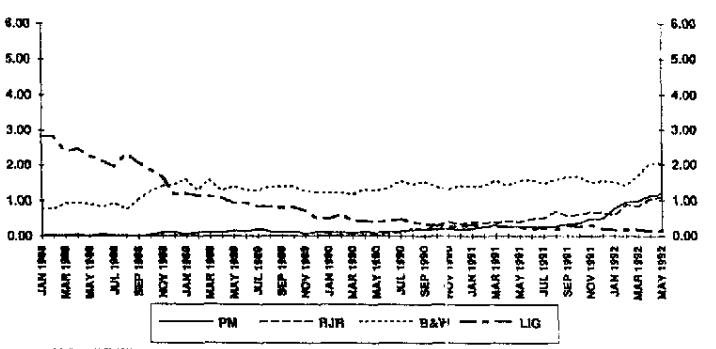
BW/PL 1MM SHARE OF INDUSTRY
CONVENIENCE OUTLETS



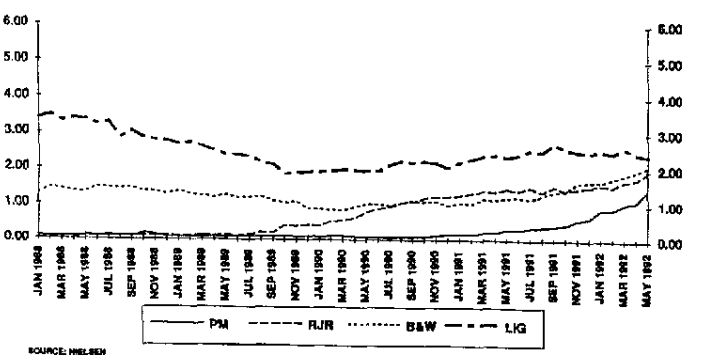
BW/PL 1MM SHARE OF INDUSTRY
GROCERY OUTLETS



BW/PL 1MM SHARE OF INDUSTRY
DRUG OUTLETS



BW/PL 1MM SHARE OF INDUSTRY
SUPERMARKETS



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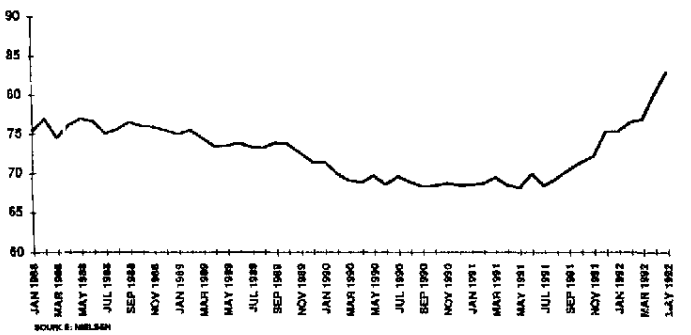
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

DISTRIBUTION:

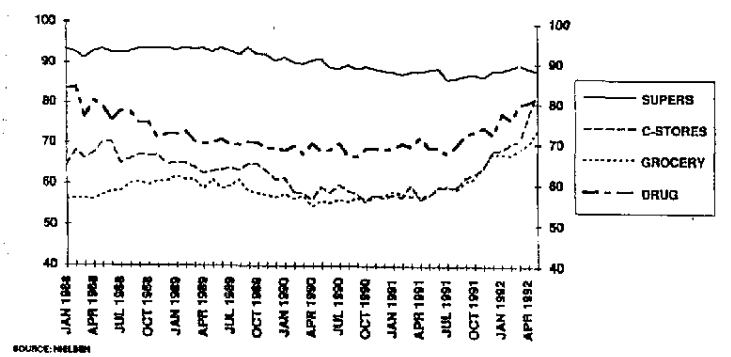
National BW/PL distribution continues to surge, gaining +6% from March levels to 83%. Geographically, the largest gains were in Region 2, (up +12% to 81%), and in Region 3, (up +8% to 93%). Region 3 is now the best developed BW/PL Region in terms of distribution.

In the Nielsen pack outlets (Convenience and Grocery) BW/PLs have had the largest distribution gains since March, up 12% and 15% respectively.

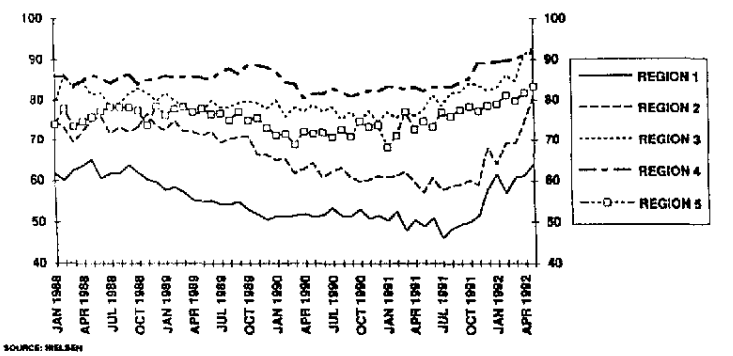
TOTAL BW/PL
1MM DISTRIBUTION (ANY PACKING)
TOTAL U.S.



TOTAL BW/PL
1MM DISTRIBUTION (ANY PACKING)



TOTAL BW/PL
1MM DISTRIBUTION (ANY PACKING)



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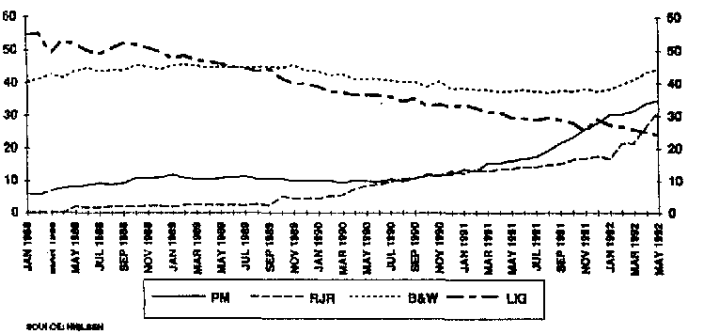
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

RJR has been a driver of BW/PL distribution increases, gaining +13% in Convenience outlets and +14% in Grocery outlets from March to May 1992. Since March 1992, RJR has also had large distribution gains in Region 1, 2 and 3 up +10%, +14% and +15% respectively. The manufacturer's apparent strategy is to take advantage of the relatively limited BW/PL distribution on the East Coast, and the strong acceptance of Discount products in Region 3.

PM has also contributed to national distribution gains, increasing +3% from March levels to 35%. Since November 1991, PM's gains have been greatest in Convenience and Grocery outlets (+6% and 3% respectively), and in Regions 3 (+8%) and 4 (+5%).

BW/PL
1MM DISTRIBUTION (ANY PACKING)
TOTAL U.S.



SOURCE: NIELSEN

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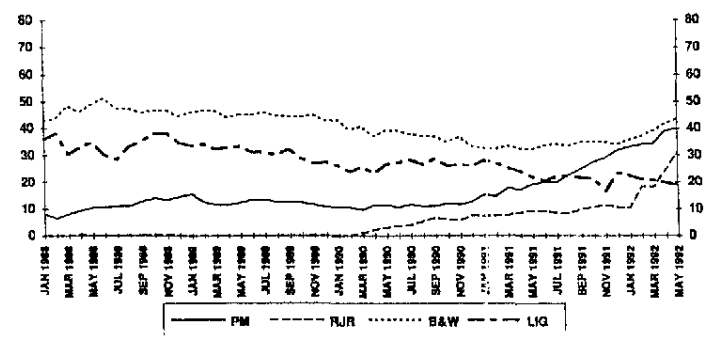
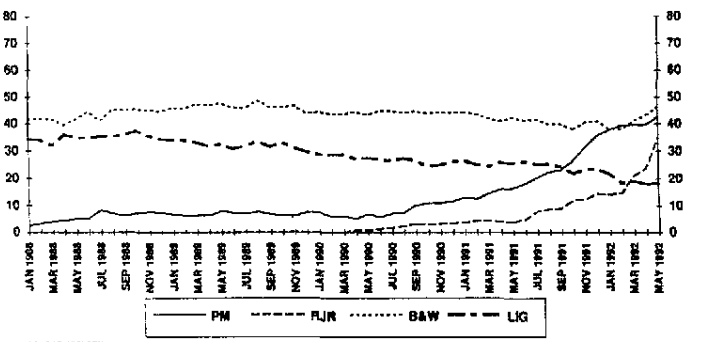
BW/PL 1MM DISTRIBUTION
IN CONVENIENCE OUTLETS



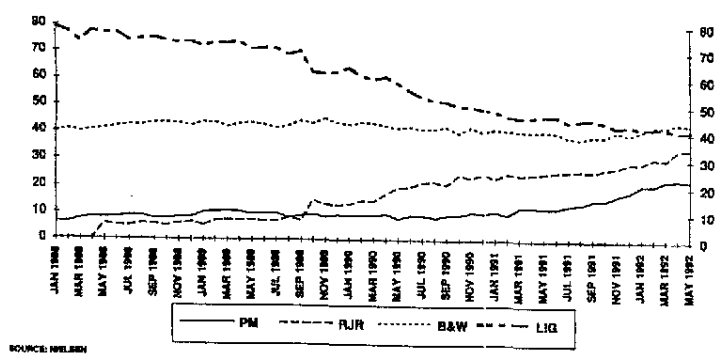
SOURCE: NIELSEN

BW/PL 1MM DISTRIBUTION
IN GROCERY OUTLETS



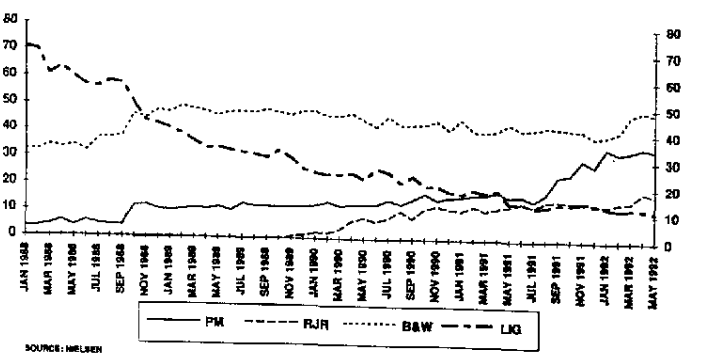
SOURCE: NIELSEN

BW/PL 1MM DISTRIBUTION
IN SUPERMARKETS



SOURCE: NIELSEN

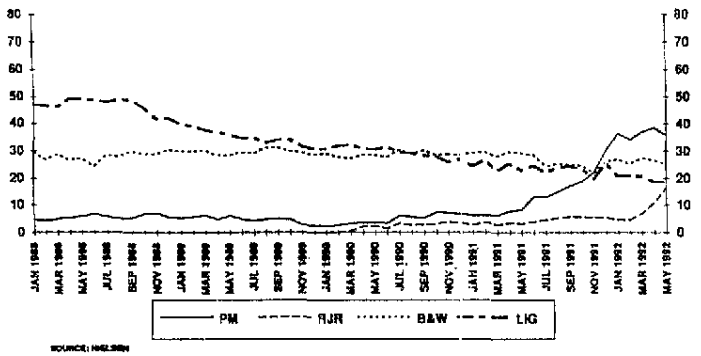
BW/PL 1MM DISTRIBUTION
IN DRUG OUTLETS



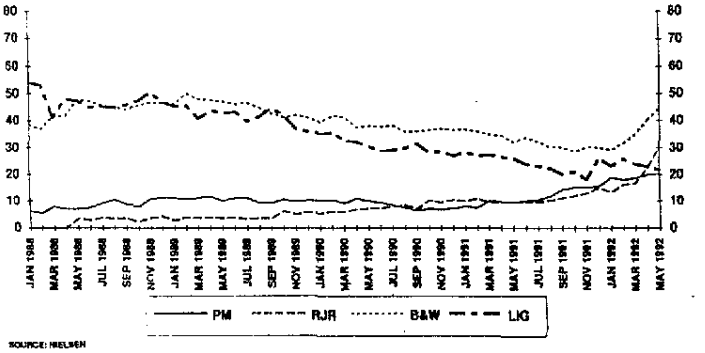
SOURCE: NIELSEN

Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

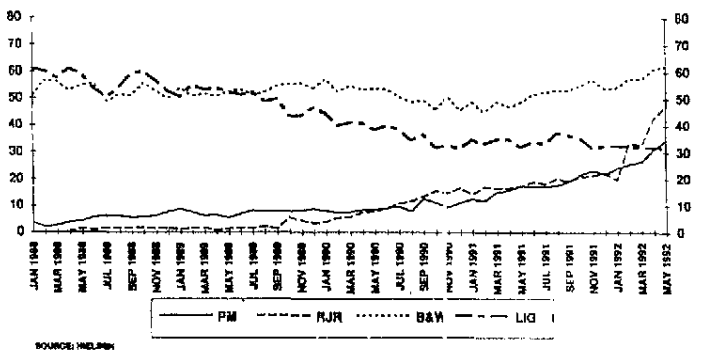
BW/PL 1MM DISTRIBUTION
IN REGION 1



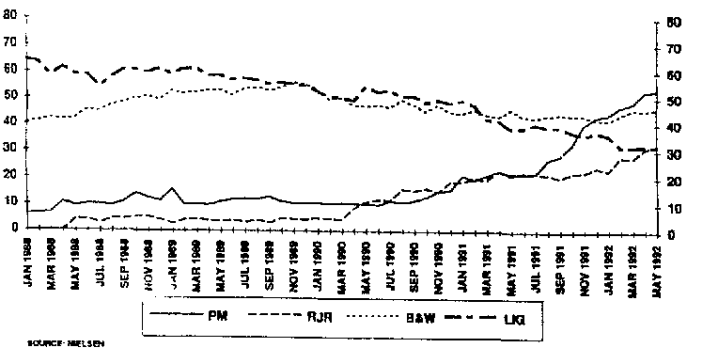
BW/PL 1MM DISTRIBUTION
IN REGION 2



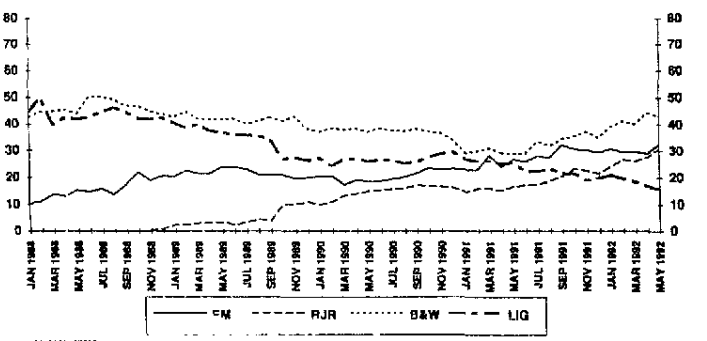
BW/PL 1MM DISTRIBUTION
IN REGION 3



BW/PL 1MM DISTRIBUTION
IN REGION 4

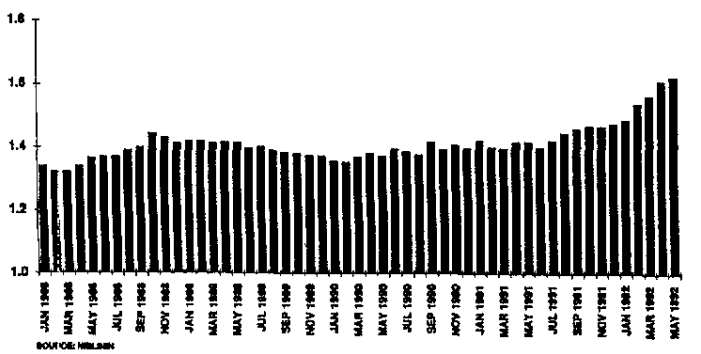


BW/PL 1MM DISTRIBUTION
IN REGION 5



Distribution gains have not only increased the number of retailers carrying the price point, but they have also increased the average number of BW/PLs per outlet. By May 1992 the average number of BW/PL manufacturers per outlet was 1.6, up from 1.4 in May 1991.

AVERAGE NUMBER OF BW/PL MANUFACTURERS
PER OUTLET CARRYING BW/PLS



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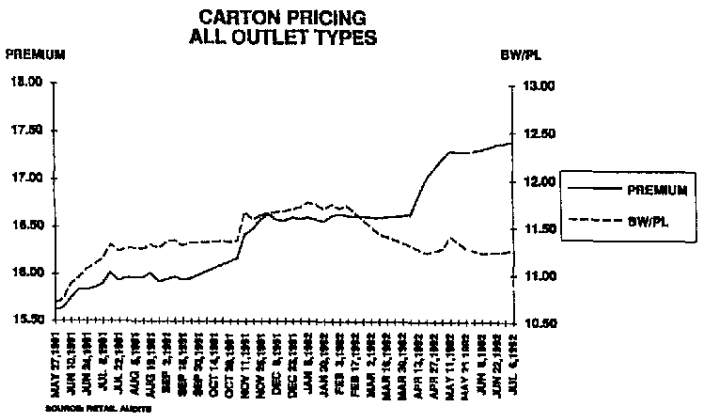
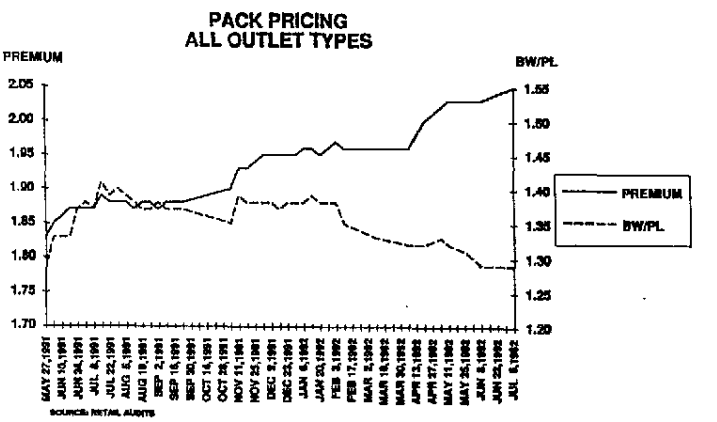
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

RETAIL PRICING

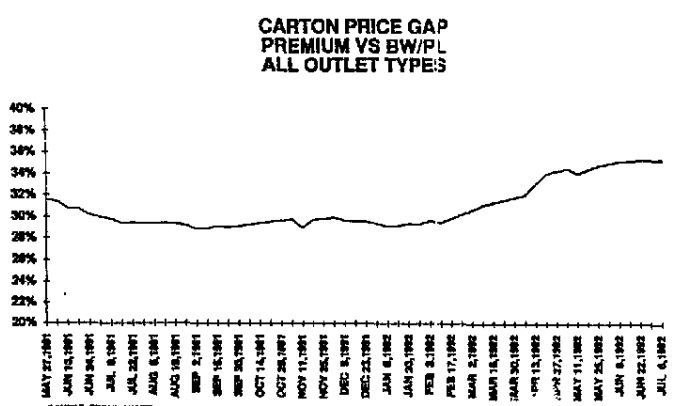
Increased retailer competition, competition among BW/PL manufacturers and among wholesalers, and the pricing simplification of Best Value and Basic have all contributed to the decline of retail BW/PL prices from February to June 1992. According to retail audits in all trade classes, average retail carton prices increased +$0.04/carton, and pack prices stabilized in late June/early July 1992.

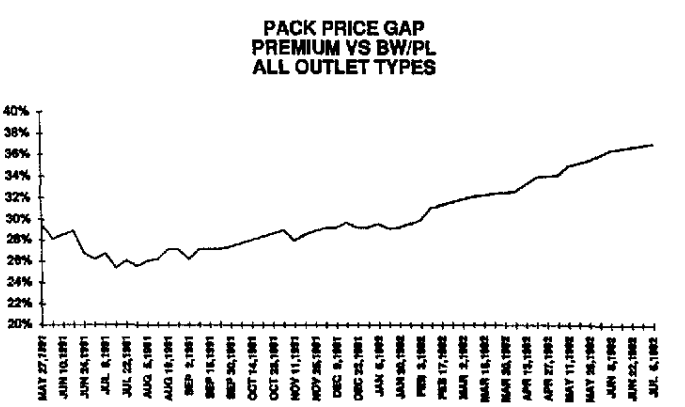
Expected distribution gains for Monarch and Private stock may also exacerbate pricing declines. As these brands develop they will either increase the number of retailers carrying the BW/PL price point, or they will increase the number of BW/PL per outlet. In either case, BW/PL downward retail price pressure will increase.





The recent BW/PL carton price increase and pack price stability have not decreased the price gap between Premium and BW/PL prices. The carton price gap has stabilized at 35%, and the pack gap continues to increase, rising to 37% in the week of 7/6/92.





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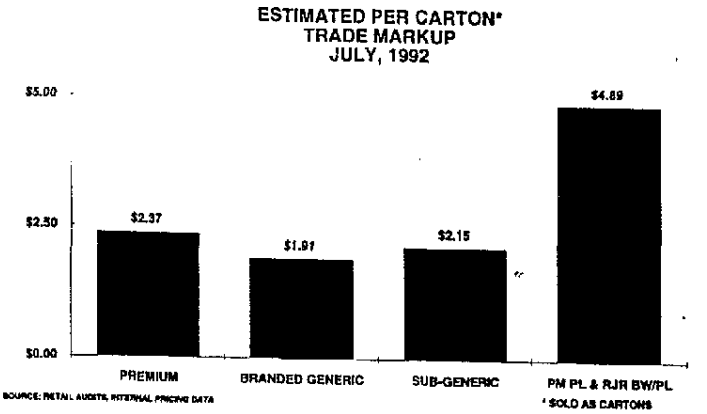
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

TRADE PROFITABILITY

Despite declining retail prices, BW/PLs continue to be the most lucrative tier for the trade to handle, with mark-ups twice that of Premiums.



BW/PLs are the least expensive products to the trade, but net cost to the trade varies from brand to brand. Manufacturers differ in the amount of allowances provided, the timing of the allowance payments, and the trade party (retail or wholesale) to whom the payment is made. The following outlines pricing to the trade, excluding wholesaler to retailer markups.

BW/PL NAME		CARTON PRICING
BASIC	List Price	$5.32
	Quarterly allowance to Distributor	-$0.50
	Quarterly Retail Merchandising Support Allowance	-$0.50
	Net Cost to Trade	$4.32
PM PRIVATE LABELS	List Price	$5.32
	Off invoice trade discount	-$0.50
	Monthly payment to private label holder	-$1.10
	Net cost to trade	$3.72
MONARCH/ BEST VALUE	List Price	$5.32
	Weekly payment to wholesaler	-$0.50
	Retailer monthly allowance	-$0.50
	Monthly "Disruption" fee paid to Retailer	-$0.60
	Net Cost to Trade	$3.72

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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

PRIVATE STOCK	List Price	$5.32
	Off invoice trade discount	-$1.35
	Wholesaler annual profit sharing	-$0.25
	Wholesaler introductory allowance	-$0.25
	Net Cost to Trade	$3.47
GPC	List Price	$6.32
	Price Reduction to Direct Purchaser	-$0.20
	Quarterly allowance to Direct Purchaser	-$0.20
	Retailer Promotion Fund	-$1.15
	Net cost to trade	$4.77

MANUFACTURER PRICING OVERVIEW

RJR

RJR's BW/PL pricing is focused on the retailer, giving $1.10 of its $1.60/carton trade allowance to the retailer. The apparent intent is to entice a retailer to display RJR's brands more prominently and price them more competitively than other BW/PL offerings in the store because they are more lucrative.

PM

Although PM's total trade payments under its Wholesale Private Label Program are the same as RJR's ($1.60/carton), PM focuses on wholesalers. PM pays the entire $1.60/carton to the wholesalers while RJR gives $1.10 to retailers and $0.50 to wholesalers.

Theoretically, wholesalers could pass much of their PM trade discounts on to retailers, making their PM Wholesaler Private Label (PM/WPL) brand competitive at retail with Monarch, Best Value, or GPC. However, if wholesalers were to pass along enough of a discount to the retailers to match RJR's retail payment ($1.10) the wholesalers profit ($0.50) would be the same as it is for Monarch, and would not compensate the wholesaler for having incurred marketing expenses.

PM's Basic is at a greater pricing disadvantage than PM/WPLs, since its total trade discounts are only $1.00, making it $0.60 more expensive to the trade.

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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

B&W

B&W's GPC pricing structure is unique among the BW/PL brands because its list price is $1.00 higher than the other BW/PLs. Additionally, although B&W pays the retailer $1.15/carton, ($0.05/carton more than RJR), expressed as a percentage of the list price, B&W's payout to the retailer is slightly lower than RJR's (18% vs. 21%). After all discounts and allowances are considered, GPC is the most expensive BW/PL to the trade at $4.77.

To offset this net pricing disadvantage, where necessary, B&W supports the brand with coupons and discounts. In geographies marked by limited price competition, B&W has the flexibility to not coupon GPC, and still have the lowest priced product in the store. Such an approach maximizes the efficiency of B&W's pricing strategy, couponing on an as needed basis. Nevertheless, because of B&W's small sales force and the logistics of continually couponing, in some outlets where continual couponing is necessary, GPC may be at a net price disadvantage relative to other BW/PL brands.

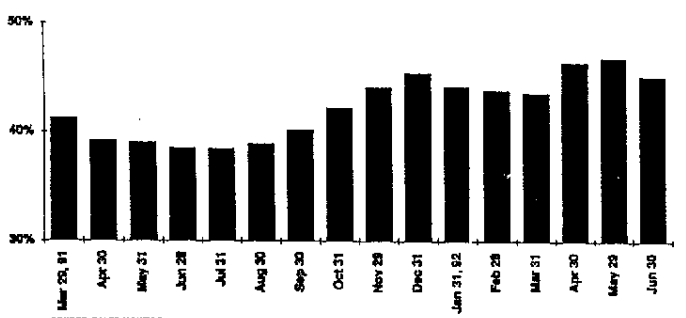
AMERICAN

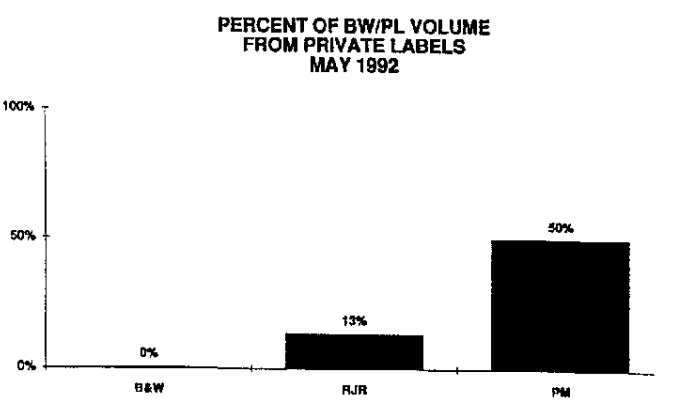
Because it is also has a "wholesaler" pricing structure, American's Private Stock faces the same shortcomings as PM's wholesaler private labels in terms of competitiveness with RJR's BW/PLs at retail.

BW/PL BRAND PERFORMANCE

Although total PM BW/PL shipments continue to be dominated by Basic and AAV, due to their more favorable pricing structure, PM's private labels are becoming an increasingly important component of its total BW/PL mix. In June 1992 (3mm) Private Labels were 45% of PM BW/PL shipment volume, up from 38% the prior year.

In May 1992, 50% of PM's retail BW/PL volume was from Private Labels versus 13% of RJR's, and 0% of B&W's.





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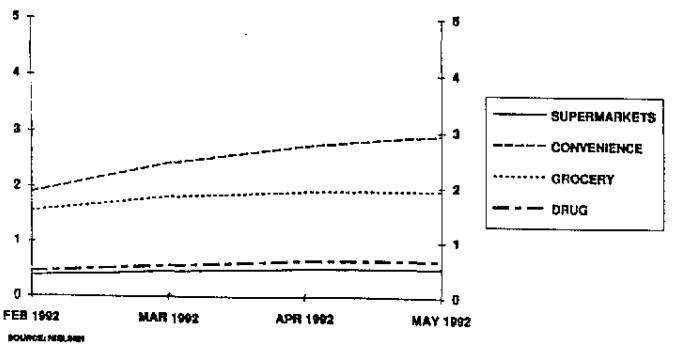
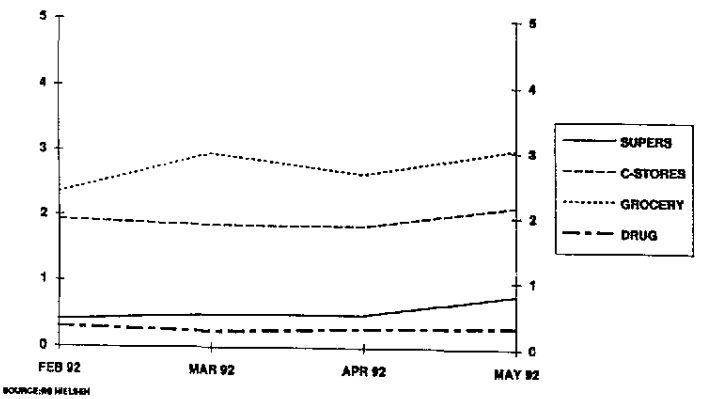
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

At retail PM's BW/PL gains in Convenience outlets have been driven by Private Labels, not by Basic. Similarly, Private Labels have been responsible for growth in Regions 1 and 3, while Basic dominates PM BW/PL volume in Regions 4 and 5. Neither Basic nor PM Private Labels are well developed in Region 2.

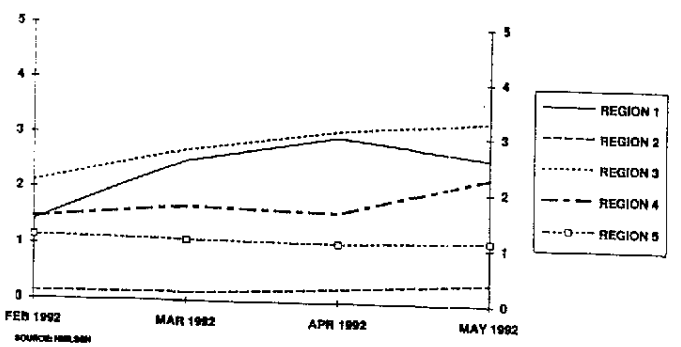
TOTAL PM PRIVATE LABEL
1MM SHARE



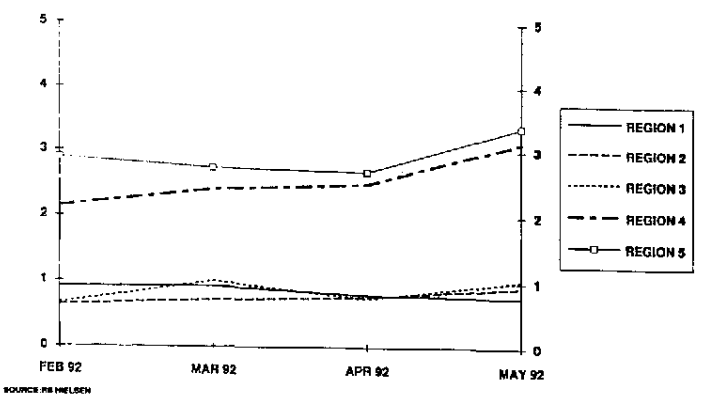
BASIC
1MM SHARE OF INDUSTRY



TOTAL PM PRIVATE LABEL
1MM SHARE



BASIC
1MM SHARE OF INDUSTRY



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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

Brand loyalties appear to be building in the fourth tier. The BW/PL segment has become dominated by a few large BW/PL brands: in May 1992, 63% of retail BW/PL volume was from Basic, Best Value, and GPC. Furthermore, Consumer Research shows 48% of all BW/PL smokers identify their brands by name rather than as a store brand, or a Generic.

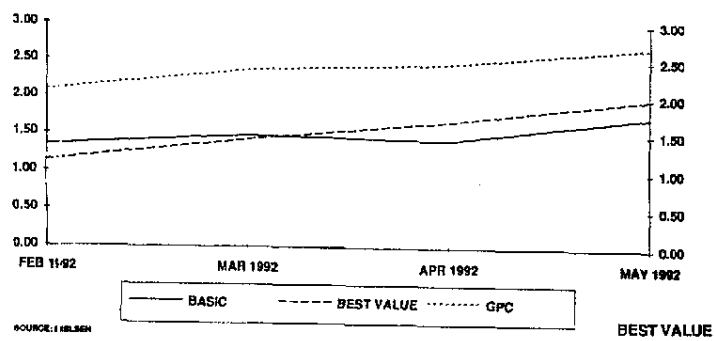
RJR is encouraging the branding of the fourth tier with the development of Monarch. The brand has attractive packaging, and its name does not have any connotations of being a "cheap" cigarette.

Not only is RJR innovative in creating an attractive "brand" Monarch, but it is also aggressive in approaching the BW/PL segment as it exists today. By driving Best Value distribution, RJR is competing head on with other large BW/PL brands which have simple packaging, and a name that suggests value. RJR has been pushing Best Value volume, and the brand has gained +0.9 share points at retail since February. Gains for the brand have been strongest in the pack outlets, Convenience and Grocery, gaining +1.1 points in each of these trade classes.

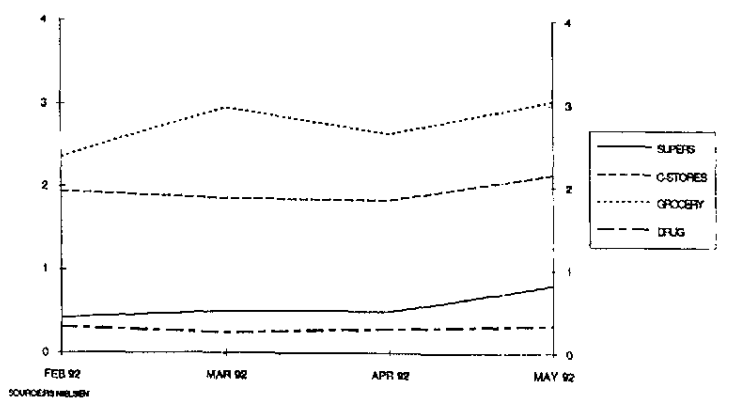
Note that although Basic and Best Value are growing more rapidly than GPC, GPC is the largest BW/PL brand.

Although no retail share information is currently available, wholesaler shipment data show Monarch share at 0.3 in the week of 6/26/92.

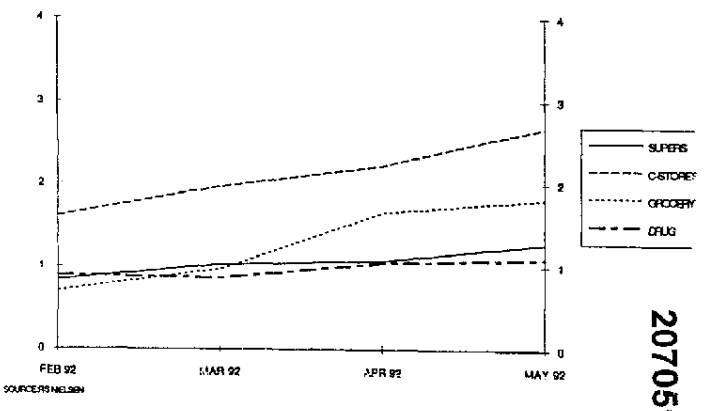
BW/PL BRANDS
1MM SHARE OF INDUSTRY
TOTAL U.S.



BASIC
1MM SHARE OF INDUSTRY



BEST VALUE
1MM SHARE OF INDUSTRY



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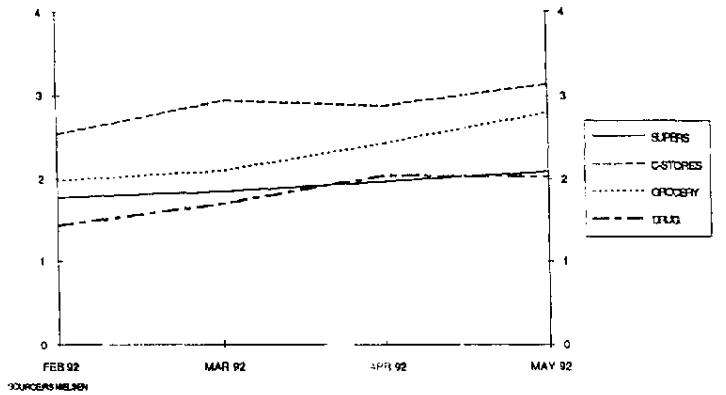
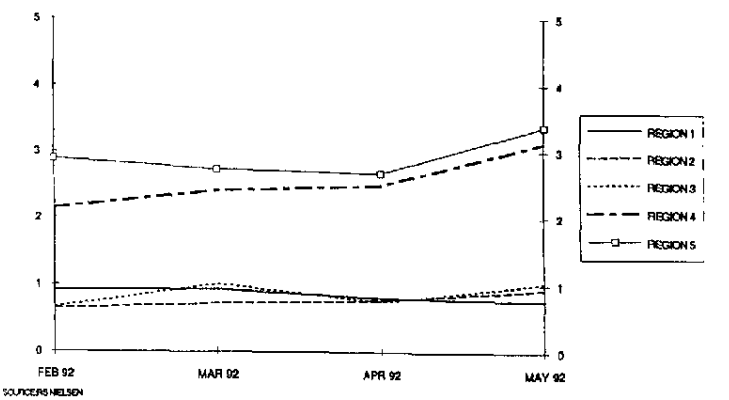
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

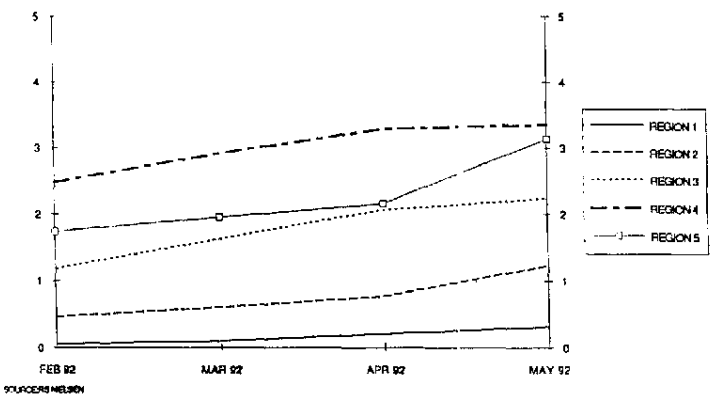
GPC
1MM SHARE OF INDUSTRY



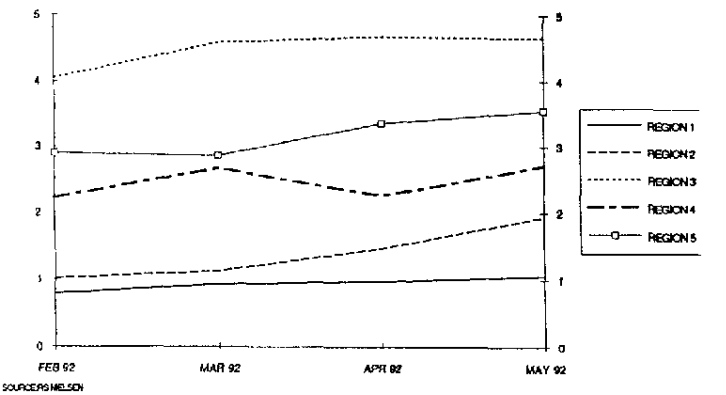
BASIC
1MM SHARE OF INDUSTRY



BEST VALUE
1MM SHARE OF INDUSTRY



GPC
1MM SHARE OF INDUSTRY

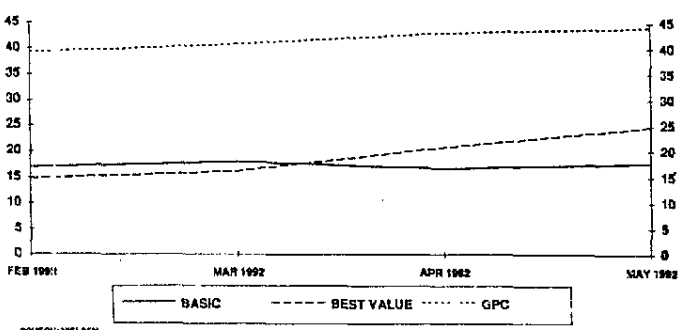


RJR's drive on Best Value is particularly evident in the brand's distribution gains. RJR appears to be focusing on pack outlets (Convenience and Grocery) its best developed BW/PL trade classes, and in Regions 1,2, and 3, where Best Value has been under-developed.

As revealed in retail audits, RJR appears to have adopted the same distribution strategy for Monarch as it has for Best Value. Although Monarch's national distribution was a low 3.5% in the week of 7/6, it appeared to be focused in Convenience outlets (8% distribution).

GPC enjoys the highest level of distribution of the BW/PL brands. Its strength is particularly evident in Region 3.

BW/PL
1MM DISTRIBUTION (ANY PACKING)
TOTAL U.S.



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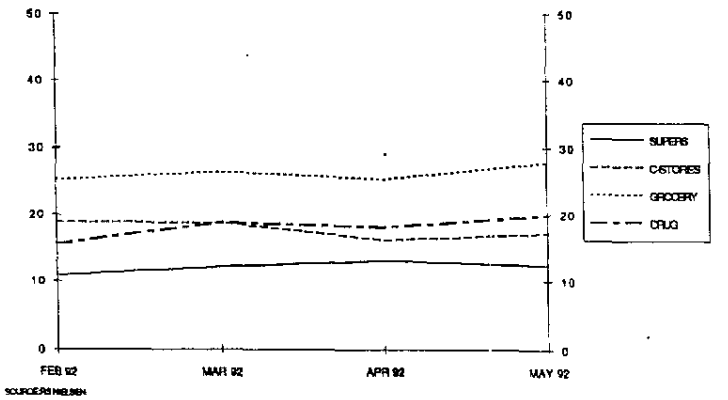
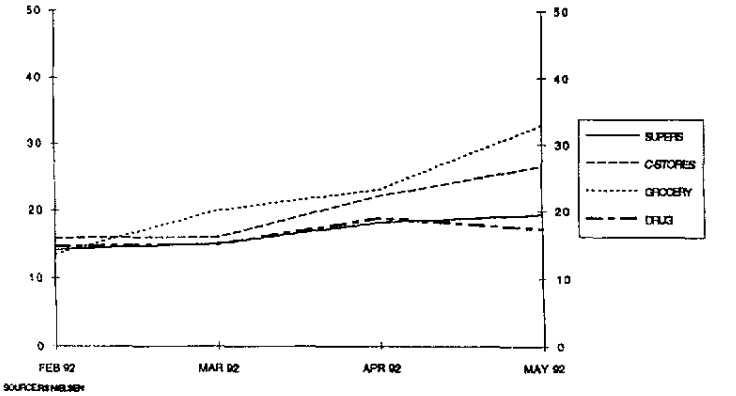
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

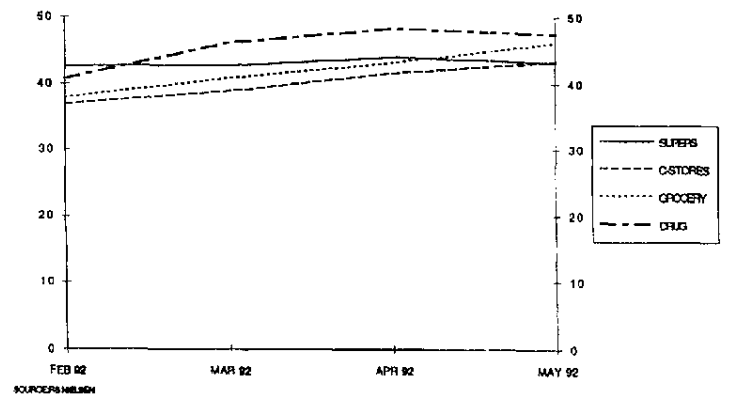
BASIC
1MM DISTRIBUTION



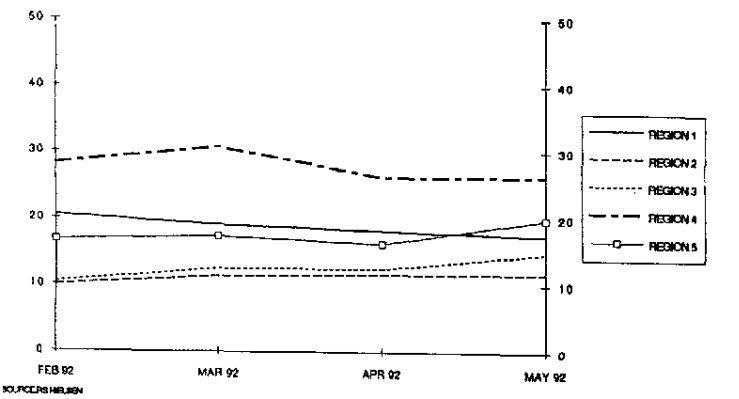
BEST VALUE
1MM DISTRIBUTION



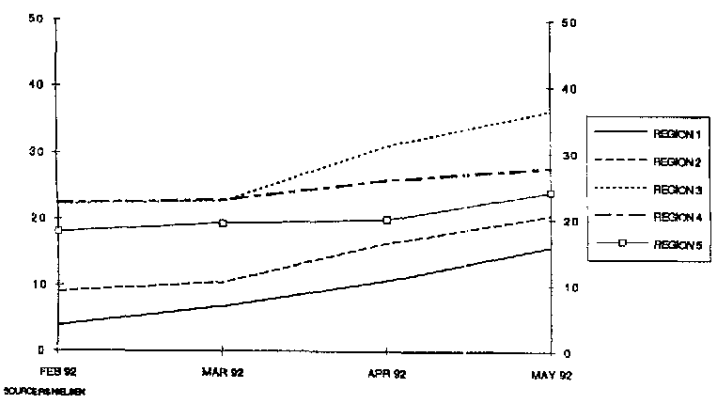
GPC
1MM DISTRIBUTION



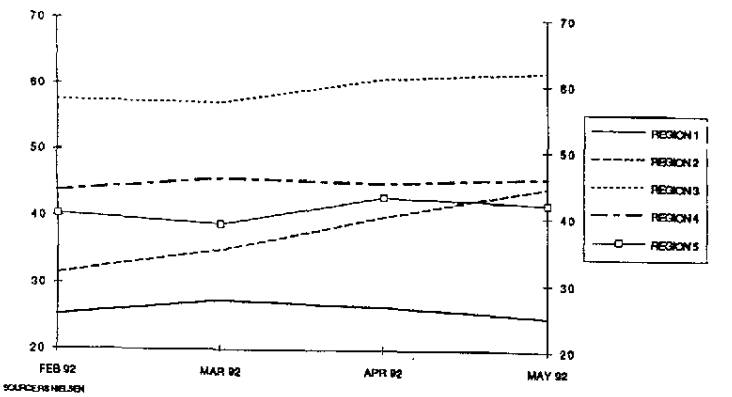
BASIC
1MM DISTRIBUTION



BEST VALUE
1MM DISTRIBUTION



GPC
1MM DISTRIBUTION



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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

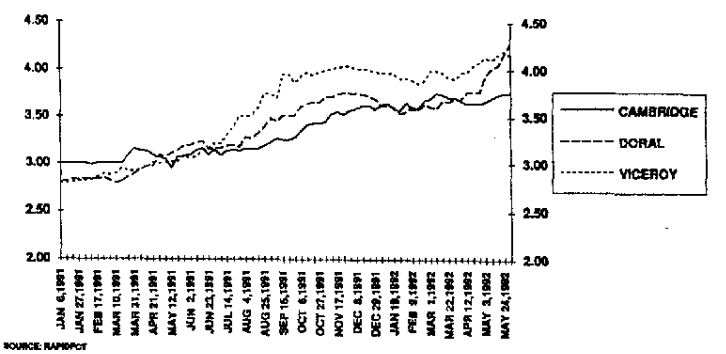
INDUSTRY DYNAMICS

To defend against losses to BW/PLs, some manufacturers have increased coupon values on Branded and Sub-Generic brands. From March to May, RJR accelerated coupon values of Doral, Magna and Sterling, and in July, it repositioned Doral to Sub-Generic. The strategy behind the value acceleration and repositioning may have been to insulate existing Discount franchises against cannibalization from the Monarch roll-out, and defend against losses to other manufacturer's BW/PLs.

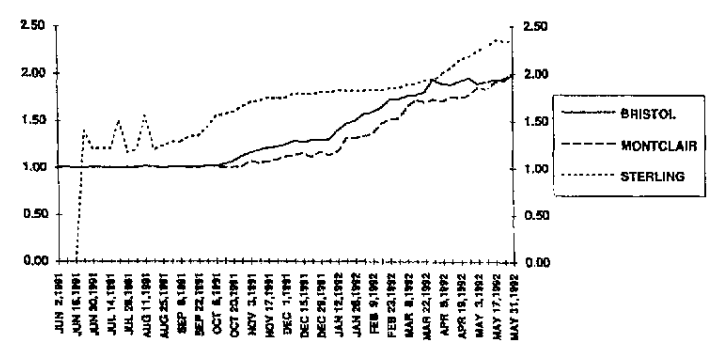
Doral's higher dollar values prompted its competitive Branded Generics, Cambridge and Viceroy to increase their dollar values. Cambridge values increased +$0.05 from March 29 levels to $3.76 by May 31, and Viceroy's were up +$0.26 to $4.16. Nevertheless, both values fell below Doral's $4.28.

Similarly, American Tobacco, which did not launch its Black & White brand "Private Stock" until the end of June, has increased dollar value and availability of discounts on Montclair. Historically, Montclair's average coupon value had been below that of Bristol. In May 1992, American increased the brand's coupon dollar values such that by the end of May, Montclair's average edged out Bristol's. In addition, although until January 1992, availability of Bristol and Montclair on carton coupons were similar, availability of Montclair coupons jumped in January 1992. By May 1992, 55% of Scanning Supermarkets had Montclair discounts versus 44% for Bristol.

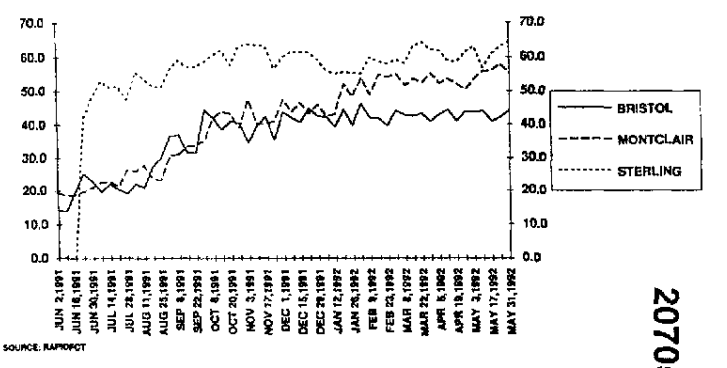
AVERAGE CARTON COUPON VALUE
IN SCANNING SUPERMARKETS



AVERAGE CARTON COUPON VALUE
IN SCANNING SUPERMARKETS



PERCENT OF STORES WITH IRCS
IN SCANNING SUPERMARKETS



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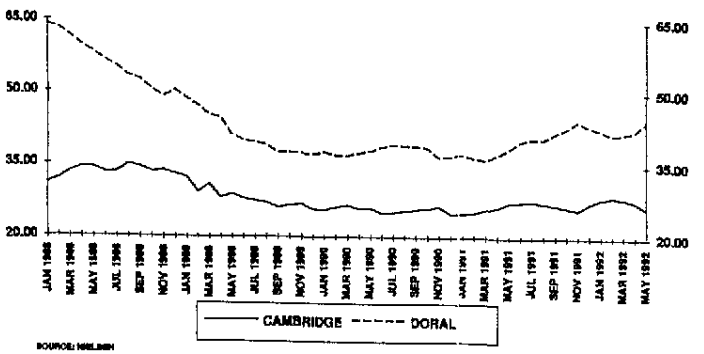
Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004

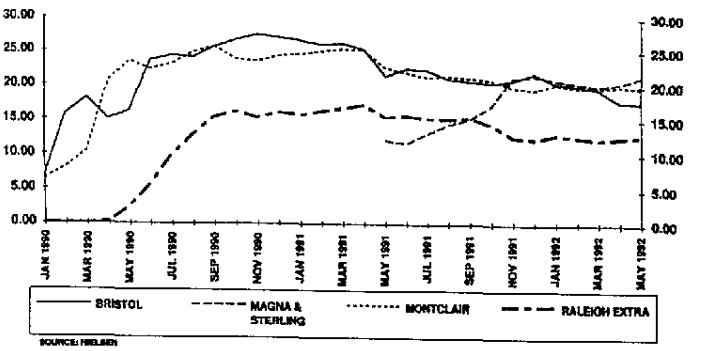
RJR's and American's strategies appear to have been successful. Although the Sub-Generic and Branded Generic categories lost share since March, due to RJR's and American's aggressive discounting, their brands' declines have under-indexed their respective categories'.

Doral's share of Branded Generics has increased +2.5 to 44.3, while Cambridge, which did not accelerate coupon values as rapidly, has lost -2.1, falling to 26.2. Similarly, Magna and Sterling increased their share of Sub-Generics +1.4 since March, while Montclair maintained its share at approximately 20, and Bristol share fell -2.0 to 17.6. Bristol's relative weakness may reflect the combination of less competitive national discounting and vulnerability in Region 3 where BW/PL distribution is highest.

BRANDED GENERICS
1MM SHARE OF SEGMENT

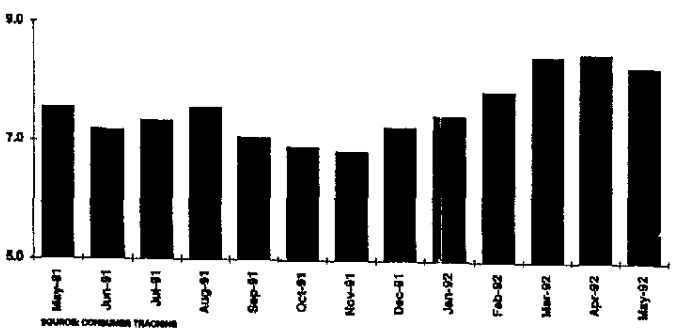


SUB-GENERICS
1MM SHARE OF SEGMENT

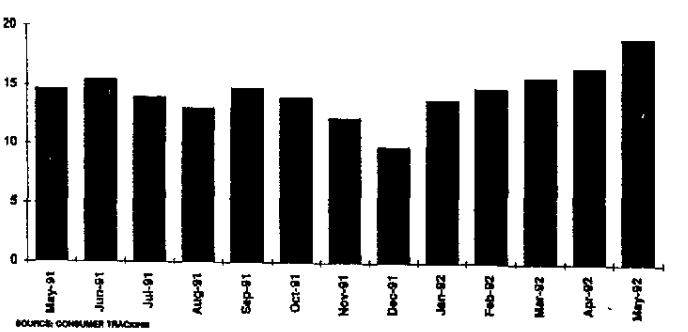


The price competition at the low end appears to have had an impact on Marlboro. Its inter-brand alternate purchase rate has increased in 1992, and BW/PLs have captured a larger portion of its alternate volume.

MARLBORO
INTER-BRAND ALTERNATE PURCHASE RATE
3MM



BW/PL
SHARE OF MARLBORO ALTERNATE VOLUME
3MM



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Source: https://www.industrydocuments.ucsf.edu/docs/qqmm0004